Service Date: December 30, 1998

DEPARTMENT OF PUBLIC SERVICE REGULATION
BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MONTANA

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IN THE MATTER OF MONTANA-DAKOTA UTILITIES CO., Application for Approval of a Transportation Service Agreement	))))	UTILITY DIVISION DOCKET NO. D98.11.274 ORDER NO. 6133a

FINAL ORDER

1. On November 17, 1998, Montana-Dakota Utilities Co. (MDU) filed before the Public Service Commission (PSC) an application for approval of a proposed transportation service agreement with Cenex Harvest States Cooperative (Cenex). MDU's application was noticed for public participation purposes as a notice item on the PSC's weekly business meeting agenda for the week of December 14, 1998. No comments or inquiries were received by the PSC.

2. In the MDU / Cenex service agreement MDU proposes to deviate from the floor price under MDU Transportation Service Rates 81, 82, and 84, to avoid possible bypass of MDU facilities by Cenex (i.e., to retain transportation throughput). MDU's current tariffed floor price is $0.101 per dk. MDU's proposed rate in the MDU/Cenex transportation service agreement is $0.06 per dk. MDU is currently charging Cenex $0.115 per dk. The proposed rate is above MDU's marginal cost of providing service to Cenex on a stand-alone basis.

3. Several past MDU proceedings before the PSC have shaped gas costing and pricing policies for MDU. A brief description accentuates the PSC’s approach in analyzing MDU's present application. In Docket No. D85.7.30 the PSC’s costing policy held that, because utility regulation seeks to emulate the results of competition for an industry characterized by a monopoly, marginal cost pricing recommends itself in the design of gas prices. In that docket the PSC granted MDU’s request for margin-based interruptible transportation prices pending “a more desirable method to compute transportation prices."

4. In MDU Docket No. D87.1.8 the PSC found merit in supporting flexible pricing.

However, the PSC approved MDU’s pricing proposals on a short-term basis of 15 months. Longer-term approval required knowledge of the relevant cost / price constraints and revenue impacts. In that docket the PSC determined that, absent an approved marginal cost study, the price floor of $0.05 would remain in effect for a period not to exceed 15 months. The PSC also found that continued flexibility would be granted only upon MDU’s filing a long-run marginal cost study for services, especially for Rates 81, 82, and 90. If not filed, all transportation service tariffs would have had to revert to the last tariffed "margin" based prices.

5. In April 1989 MDU filed Docket No. D89.4.14, clarifying its base rate language on its firm and interruptible transportation tariffs, which the PSC approved in August 1989. In its decision, the PSC expressed concern, among others, with MDU’s lack of cost-support data.

6. In the present matter, MDU asserts that Cenex has not accepted any transportation service from MDU since April 1998 for the following reasons: 1) the total burner tip price on MDU’s system is higher than that of Cenex's alternative natural gas supplier; 2) the price for the Cenex refinery’s propane has been depressed for most of the year due to the regional oversupply (allowing Cenex to use propane as an alternative fuel); and 3) Cenex has been fulfilling a contractual minimum volume commitment with Cenex's alternative natural gas supplier (according to Cenex, this commitment has, or is about to, expire).

7. MDU states that it attempts to obtain the tariff-ceiling rate in order to maximize benefits to MDU and its firm service customers. However, as the present MDU / Cenex situation illustrates, when faced with potential loss of load due to bypass or competition from an alternate fuel source (i.e., Cenex is currently able to receive transportation service from MPC and has the ability to produce and burn propane on site), MDU will attempt to reduce MDU's transportation rate to retain customers. MDU has five Rate 82 customers taking service at less than the current ceiling rate.

8. It appears that MDU has supplied Cenex, over the past 4 years, on average of about 436,000 dk per year. This figure is an estimate because 1998 usage is only through October of this year. Therefore, over five years, the proposed MDU/ Cenex transportation service agreement would substantially increase the annual amount of gas transported by MDU to Cenex.

9. Given the above-mentioned transportation and fuel alternatives and absent a rate-concession approval by the PSC, MDU believes that Cenex will pursue a bypass of MDU's distribution facilities. MDU claims that a bypass of MDU facilities will result in, on the margin, an annual loss of $62,880. Additionally, MDU states that the potential revenue loss, if Cenex were to bypass, would not cause MDU to file a rate case at this time, but, in a future rate case, MDU will claim the volumes and revenues would reflect that Cenex was no longer a customer. Yet, in response to PSC-001(b) (a data request in the present docket), MDU states, assuming that the $0.06 per dk for Rate 82 service is denied, "the loss will be a factor in the Company's ability to earn an adequate return on its investments and will, through a future rate case process, result in increased prices to the other customer classes." In a staff conference call, MDU was asked what Cenex's test year sales were in MDU's last cost of service/rate case - Docket No. 95.7.90. Don Ball, in MDU regulatory affairs, stated that there were no test year sales for Cenex during that docket. Therefore, MDU's assertion that if this agreement is not approved MDU will experience a $62,880 annual loss is not a loss that stems from test year sales and revenues MDU was authorized to collect out of Docket No. D95.7.90. The $62,880 is not a reduction in revenues, rather, other things being equal, it is an opportunity cost to MDU to collect additional revenues over and above what were approved and allowed in Docket No. D95.7.90.

10. The PSC determines that MDU's application should be approved. However, the following conditions apply: 1) all sales under the MDU / Cenex agreement are interruptible as opposed to firm; 2) no capital investment is needed to execute the MDU / Cenex agreement, as Cenex already has facilities connected to the interstate pipeline; and 3) the $0.06 per dk price floor is based on the individual marketing agreement between Cenex and MDU and in no way reflects an economic analysis by the PSC.

11. The PSC approves MDU's request to deviate from the current tariffed price floor in its agreement with Cenex. Over the next five years MDU will transport for Cenex a minimum of 5,000,000 dk of natural gas. The agreement calls for Cenex to transport at a rate equal to $0.06 per dk, $0.041 below the current price floor. The PSC is not satisfied that the price floor rate equal to $0.06 per dk is economically sound. In its next cost of service / rate case, MDU's marginal cost data for Rate 82 service will be analyzed by the Commission.

Done and dated this 22nd day of December 1998, by a vote of 5-0

BY ORDER OF THE MONTANA PUBLIC SERVICE COMMISSION

DAVE FISHER, Chair

NANCY MCCAFFREE, Vice Chair

BOB ANDERSON, Commissioner

DANNY OBERG, Commissioner

BOB ROWE, Commissioner
(Concurring opinion included)

ATTEST:

Kathlene M. Anderson
Commission Secretary

(SEAL)

NOTE: Any interested party may request the Commission to reconsider this decision. A motion to reconsider must be filed within ten (10) days. See 38.2.4806, ARM.

CONCURRING OPINION OF COMMISSIONER ROWE

Based on the analysis underlying this order, substantial concerns could be raised about any similar requests if filed prior to MDU's next rate case.

RESPECTFULLY SUBMITTED this 22nd day of December, 1998.

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BOB ROWE, Commissioner